MONDAY MATTERS

NOBLE PLANNING

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What' in today's special President's Day Tuesday edition:

- Is the Market Pendulum Swinging Back?
- Weekly Economic Cheat Sheet
- Three Technical "Cs" for a Lasting Market Bottom
- Is This Another Bull Trap?
- What the CPI Means for Markets

Stock futures are lower while the dollar and Treasury yields move higher as part of a continuation of last week's hawkish money flows, partially thanks to strong data overnight.

Economically, the EU Composite PMI jumped to 52.3 vs. (E) 50.7 due to strength in the service sector, bolstering expectations for increasingly aggressive monetary policy in the months ahead which is weighing on risk assets globally this morning.

As far as other catalysts go, there are no Fed officials scheduled to speak but there is a 2-Yr Treasury Note auction at 1:00 p.m. ET and if yields continue higher in the wake of the auction, expect more pressure on stocks, especially higher valuation/growth names.

Finally, earning season is winding down but a pre-market release by WMT ($1.52) should shed some light on the health of the consumer and could impact markets as well.

Market	Level	Change	% Change
S&P 500 Futures	4,053.00	-34.50	-0.84%
U.S. Dollar (DXY)	103.9600	0.0980	0.09%
Gold	1,843.40	-6.80	-0.37%
WTI	76.77	0.43	0.56%
10 Year	3.892%	0.064	1.68%

Planning Corner

Filing deadline for NJ property tax relief was extended to February 28. Many people are unaware that they are eligible for this tax relief payment because of the stop-and-go history of NJ tax relief programs. This program is called NJ Anchor for eligible NJ homeowners and renters:

NJ homeowners with income of $150,000 or less will receive $1,500.

NJ homeowners with income of more than $150,000 and up to $250,000 will receive $1,000.

NJ residential renters with income of $150,000 or less will receive $450. You must have paid rent to be eligible.

Check out this website or contact our office to help you understand how to apply

https://www.state.nj.us/treasury/taxation/anchor/index.shtml

Call to schedule an appointment.

(201) 350-8461

Stocks

Last Week (Needed Context as We Start a New Week)

Stocks fell to new lows for the month last week amid higher-than-expected inflation data and increasingly hawkish Fed commentary. The S&P 500 ended the week down 0.28% leaving the index up 6.24% YTD.

The week started with solid gains last Monday as stocks tracked overseas markets higher early after the European Commission raised growth forecasts and lowered inflation expectations for 2023, boosting optimism for a soft/no landing. Stocks continued higher on the back of a record decline in wage expectations within the New York Fed's consumer survey report, which further bolstered hope for a soft landing. The S&P 500 advanced 1.14%.

Volatility began to pick up Tuesday as stocks reversed tentative early gains to give back all of Monday's rally as a moderately hotter-than-expected CPI release (across the board including revisions) sent terminal rate expectations beyond 5%. The market rebounded in the afternoon after the Fed's Harker said the FOMC "is not done yet but they are likely close," and that saw the S&P recover to end just 0.03% lower on the day.

The market remained stable on Wednesday as investors digested a strong Retail Sales report that showed consumer spending remained healthy at the start of 2023 while the Empire State Manufacturing Survey was better than feared, once again rekindling hopes for a soft landing despite the steady flow of hawkish Fed chatter over the course of the week. The S&P 500 bounced 0.28%.

The market came back for sale on Thursday after PPI ran hot, the Philly Fed headline badly missed estimates (and had rising price measures), jobless claims remained stubbornly below 200K and Housing Starts data slowed twice as fast as expected to start the new calendar year. Stocks extended the opening losses in early trade after Mester shocked the markets when she revealed that she thought there was a case for a 50-bps hike at the last Fed meeting. Yields peaked midmorning and opened the door for a relief rally that lasted into the afternoon until the Fed's Bullard echoed Mester's comments about 50 bps in February and didn't rule out 50-bps moves at future meetings. The S&P 500 made new lows for the week, ending down 1.38%.

For the fourth day in a row, stocks gapped lower at the opening bell on Friday thanks to German CPI coming in at 17.8% vs. (E) 16.0% while U.K. Retail Sales were unexpectedly positive, both of which resulted in more hawkish policy expectations. Fed speak continued to move markets Friday as Bowman said the latest data is not consistent with the Fed bringing inflation down towards target, but the S&P bounced when Barkin was quoted favoring a 25-bps hike in March. Some tentative dip buying in the afternoon saw the S&P 500 end near session highs, but still down 0.28%.

<u>Is the Market Pendulum Swinging Back?</u>

Stocks have enjoyed a very solid start to the new year (S&P 500 up 6.5%) thanks to two main factors: First, economic growth wasn't collapsing (i.e. no hard landing). Second, the Fed was almost done with rate hikes (which would remove a major equity market headwind). This set up led to a solid rally in stocks and bonds, which sent Treasury yields lower from the start of the year through the first week of February.

Those macroeconomic movements reverberated with market sectors. Growth styles handily outperformed and rebounded from a disastrous 2022, tech, consumer discretionary and communications services (the higher multiple, growth-oriented sectors) outperformed through January, and even once-left-for-dead meme stocks (AMC) saw solid gains as money chased returns higher on the hopes the troubles were ending.

Starting with the January jobs report, out Feb. 3, those macro ideas of no hard landing and the Fed being almost done have been challenged. That occurred again last week as economic data was mixed while numerous Fed officials reacted to firmer-than-expected inflation and economic data by floating the idea of more rate hikes.

Since that January jobs report (Feb. 3) the result has been a reversal of what occurred in January: Bond yields are up, growth is again lagging value while tech, consumer discretionary and communications services sectors are lagging defensives sectors such as utilities and consumer staples, and value. For all the different feel of this market from 2022, the above price action reveals this truth: It's basically the same market we had for most of 2022 as it's still being driven by Fed expectations, and those Fed expectations now are being driven by data.

From Jan. 1 through the February jobs report, data was better than feared and the market believed the Fed was close to ending rate hikes. Stocks rallied hard and tech/growth/high-multiple names outperformed, **just like they did when investors thought the same things in 2022 (remember buzz words "pivot" and "pause?").**

Conversely, over the past two weeks, markets are admitting the Fed may not be close to done, and they've dropped while defensive sectors and value have outperformed or relatively outperformed, just like they did in 2022 when investors had the same concerns.

Bottom line is not that much has changed. The market pendulum is still swinging between two realities: The Fed is close to done and a soft landing will happen (tech/growth/high multiple outperform as stocks and bonds rally) or the Fed isn't close to done and a hard landing might happen (stocks decline, defensives and value outperform and tech/growth gets hit hard). I remain more concerned that the Fed is not done than I am optimistic they are done.

Positively, markets have proven more resilient to swings in sentiment this year. A 50+ spike in the 2-year yield last year would have collapsed stocks. This year it's evoking a small and so far, manageable pullback. That will remain the case as long as two things stay in place: 1) Economic growth doesn't roll over hard. 2) The Fed

does not signal that terminal fed funds (the peak rate) will be substantially above the 5.125% expectation (if it goes to 5.375% the market can probably withstand that as long as growth is good, but if it's above that, brace).

Bottom line, the market has proven more resilient than last year to rising yields and that's good. But it's not immune to them and in the end we're still in a "Fed-on/Fed-off" market. And while we want to get more aggressive on the long side because we know it's a longer-term opportunity, we'd rather be a bit late than too early. As such, we remain more in favor of defensive tactical allocations and lower-volatility ETFs and factors until we really know the Fed is "done," because despite hopes that's the case, there's just not enough evidence yet.

Economic Data (What You Need to Know in Plain English)

Need to Know Econ from Last Week

Economic data last week gave a clear message on inflation and a mixed message on growth, and the net result was that rate hike expectations rose slightly and that weighed on markets especially late in the week. The most important economic data from last week were the CPI and PPI reports, and both gave the same message: Inflation is still falling, but the pace of that decline has meaningfully slowed.

The headline readings on CPI were slightly hotter than expected as headline CPI rose 6.4% y/y vs. (E) 6.2% while core CPI gained 5.6% vs. (E) 5.3%. Positively, both of those readings were slight declines from December (implying inflation pressures are still falling) but the pace of that decline slowed meaningfully. Looking further into the data, the key inflation metric, recently named "Super Core" inflation, which is core services inflation minus housing, autos and health insurance, rose 0.3% and reflected the reality that inflation pressures, while easing, remain in place.

PPI gave a similar message, as headline PPI rose 6.0% vs. (E) 5.5% while core PPI gained 5.4% vs. (E) 5.0%. Bottom line, the S&P 500 above 4,000 is pricing in a continued and consistent decline in inflation. If that does not happen, and inflation stays buoyant, the Fed will likely have to hike rates more than expected.

While inflation data was remarkably consistent, the growth data was much more mixed. January Retail Sales were strong at 3.0% vs. (E) 1.7%, while the "Control" group, which is our best measure of discretionary spending, gained 1.7% vs. (E) 1.1%, reflecting the reality that consumer spending has remained strong. But manufacturing data was mixed as Empire manufacturing showed a solid bounce as it rose to -5.8 vs. (E) -18.5 while New Orders leapt to -7.8 from -31.1. However, Philly Fed showed the opposite and dropped sharply to -24.3 vs. (E) -7.2 and New Orders declined -13.6 vs. (E) -10.9. Regional surveys are volatile and often disagree, but the level of disagreement in these two is larger than usual and underscores the confusion in the economy and market right now.

Bottom line, last week the data hinted at stagflation (buoyant prices and possibly slowing growth) and that's why stocks dropped late in the week. Now, one week's data doesn't mean much, but for a market that has aggressively bought into the idea of a "no landing," it did weigh on sentiment.

<u>Important Economic Data This Week</u>

The economic calendar remains busy this week with more important updates on growth and inflation, and if the data hints further at stagflation, as the data from late last week did, then it will weigh on stocks further. The key report this week comes tomorrow via the March flash PMIs, and the markets will want to see stability in this data. At this point, a hard landing is the most negative outcome for the markets as that's not priced into stocks, so if we see a sudden drop in the flash PMIs that will increase concerns about a sudden slowing of growth. Conversely, if the data remains resilient, that'll boost the no-landing scenario, and whether stocks can rally will depend on how quickly bond yields rise (if they don't, stocks can rebound).

The next most important report this week centers on inflation, and it's Friday's Core PCE Price Index. Some of the importance of this report has been taken away because we get CPI a week before, but the Core PCE Price Index is still the most important inflation report for the Fed, and if it's stickier than expected (as most inflation reports have been this month) that will boost expectations for a higher terminal rate and that would weigh on stocks and bonds.

In addition to those reports, we also get the FOMC minutes on Wednesday, and especially given the Mester comments from last week, markets will want to see how much support a 50-bps hike had a month ago, because if it's more than previously expected it'll increase chances for 50 bps in March (or perhaps additional hikes in June and July). Again, more hikes (and a higher terminal rate) would be a new headwind on stocks.

A continued rise in bond yields, in some cases to multi-month highs, was the key story from the space as rising yields weighed on stocks. The 2-year yield gained 8 bps last week, hit a three-month high and came within 10 bps of a 2022 high all thanks to hotter-than-expected inflation data from the U.S. (CPI and PPI) and EU (German PPI). The rise in short-term yields was warranted, as fed fund futures priced in a 50%-plus chance of a rate hike in June, which would take the terminal rate to 5.375%, 25 bps above the current 5.125% target.

That increase in the 2-year yield helped to push 10s-2s to fresh lows, near -90 bps, as the yield curve's message of an imminent and substantial economic slowdown has been remarkably steady (albeit so far incorrect) amidst all the equity and bond market gyrations. Few anticipated we'd be debating more-than-expected rate hikes in 2023, yet here we are, and it's all because of the data. Fears over these rate hikes did weigh on stocks last week, and if they become more likely, we should expect that headwind on stocks and bonds to strengthen and bring back unpleasant memories of 2022.

Special Reports and Editorial

Three Technical "Cs" for a Lasting Market Bottom

There are "three Cs" necessary for a sustainable bear market bottom to occur from a traditional technical vantage point. They are 1) Capitulation, 2) Conviction, and 3) Correlation.

Regarding capitulation, it is often a difficult concept to quantify or measure, but it is a behavior that has been a part of just about every major stock market bottom in history. On the charts, capitulation appears as an acceleration lower in prices due to the panicked nature of the selling, mostly by retail investors.

One way we can attempt to quantify capitulation is through the use of the RSI indicator, which is displayed as an oscillator (0-100) and can identify overbought (above 70) and oversold market conditions (readings below 30). Looking back to WWII, every major market bottom that followed a 20% or larger decline in the broader market has been preceded by a break below 30 in the RSI of the S&P 500 on a weekly time frame.

In 2022, that reading approached 30 twice but notably did not break below it either time. For reference, the weekly RSI of the S&P 500 fell to 20 before stocks bottomed in 2002, a reading of 16 prior to the 2009 lows, and 21 during the Covid pandemic lows; all considerably below 30. So, based on our interpretation of the charts and our historically backed measure of capitulation, the first of our three "Cs" has not yet occurred.

The second "C" is conviction, something that is most-often associated with volumes as far as technical analysis goes. We touch on the topic in the "bull trap" section (see below), but ultimately, we will need to see rising volumes with rising prices to confirm bullish conviction has returned to the market (and falling volumes on pullbacks). Until then, the market will remain susceptible to extreme bouts of volatility and the threat of new multi-year lows.

Finally, the third "C," correlation. In this instance, we are referring to derivatives markets and cross-asset analysis, particularly the typically inverse relationship between the VIX and S&P 500 during bull markets. Specifically, the fact that during bull markets new significant lows in the S&P 500 are typically met with new highs in the VIX as hedging activity picks up meaningfully. In the early to middle stages of bear markets, that relationship tends to break down as sophisticated institutional investors, or "smart money," liquidate or reduce long equity exposure and subsequently abandon the relevant and associated hedges. This results in new stock market lows not causing new relative highs in the VIX, a dynamic we saw numerous times over the course of 2022.

While a surge in the VIX will also help us identify capitulation in real-time (as it should rip to new 52-week highs), it will also help us identify a tradeable bottom. Looking back to the bottoms of the dot-com bubble, the GFC and Covid selloff, the VIX tends to peak and begin to meaningfully move lower before the bottom in stocks.

In the case of 2002, the VIX peaked over a year before the market bottomed. In 2009 it was just over four months. In 2020, it was a week (despite the unprecedented velocity in price movements across asset classes, the declines in the VIX still preceded the bottom in stocks by three days). To be clear, we haven't even seen a meaningful rise in the VIX yet, despite the peak-to-trough drawdown of more than 25% in stocks last year! To that point, the VIX pushed a reading of 90 during both the GFC and Covid panic while in 2022 it failed to breach 40.

In any event, once we begin to see evidence of a real capitulation bottom in the works via RSI falling below 30 and the VIX running to new multi-year highs (likely beyond 40), we should be able to, with a fair amount of certainty, identify the formation of a tradeable bottom as we see the inverse relationship between stocks and the VIX return to “bull market normalcy.”

Bottom line, there has been a growing chorus of analysts, strategists, and investors beginning to say that the October lows are in. But looking at the statistical facts we have not seen the technical developments consistent with just about every bear market bottom in post-war history. As we said recently, “it could be different this time” but it has rarely been profitable to bet on that concept.

Is This Another Bull Trap?

The definition of a “bull trap” is a rally in a given security beyond a notable and widely agreed upon technical resistance level, such as a previous multi-month high, that does not generate any lasting upside momentum and eventually gives way to a sharp reversal, usually down through important technical support. In simple terms, it’s a market “head fake” that catches traders off guard and results in a spike in volatility as weak-handed longs race to liquidate positions.

Bull traps are most common in bear markets when unsupported optimism by retail investors and fast-money traders eventually meets a less-supportive fundamental reality such as valuation compression, rising interest rates, or lower-than-expected earnings into which institutional investors (smart money) are continuing to reduce or liquidate equity exposure. Interestingly, bull traps are most common in the early to middle innings of a bear market.

To that point, we saw two major bull traps in the S&P 500 on the daily chart in 2022. The first occurred in late March when the S&P 500 notched two closes above the early February highs before the index rolled over to new YTD lows. The second occurred in August when the S&P 500 rallied beyond the late-May/early June highs only to reverse course again and trend sharply lower until the October, multi-year lows were established. Through the end of last year, stocks pulled back, but held comfortably above the October lows and began 2023 with a renewed rally, which ultimately carried the S&P 500 beyond the late-November/early December peak raising the all-important question: ***Is this another bull trap, or the start of a tradeable bottom?***

While the answer to that question remains to be seen and is the source of heated debate across Wall Street right now, there is one important clue that could shed some light as to whether this is another bull trap, or the start of a new bull market cycle: Volume.

Market head fakes, including bull traps, are moves that typically occur on fading or relatively low volumes, which underscores the lack of conviction behind the initial move through an important technical level and the elevated risk that it is reversed. Fading volumes occurred in both of the 2022 bear traps while the most-recent breakout in early February came on fading volumes from the late-January peak. So, if the YTD rally in stocks is going to last and the October lows are to be considered the end of the 2022 bear market, then we will need to see volumes pick up on rallies and decline on pullbacks, proving real money is entering the market.

What the CPI Means for Markets

Last Tuesday's CPI print didn't materially alter the market conversation because it largely reflected what was expected, namely that inflation is still declining, but the pace of that decline has slowed significantly. As such, stocks didn't move materially. What did move, however, was the 2-year Treasury yield and market expectations for year-end rate levels, as the peak fed funds rate firmed up around (or slightly above) 5.125% while the year-end fed funds rate now is slightly above 5.0%. That means that market expectations for year-end fed funds have surged in less than two weeks from about 4.25% (prior to the jobs report) to just over 5.00%.

The fact that didn't hit stocks is very impressive, and as we said last week, that's all because of growth expectations. Stocks have absorbed this rise in year-end fed funds because of strong growth and a belief the "no-landing" scenario is now the most likely one. As long as no landing is the market's belief, stocks will remain resilient (I don't think that's enough to push the S&P 500 materially higher from here, but it should keep pullbacks mostly limited to 5% or less).

This means the key for markets going forward remains economic growth, and that's the main takeaway from the in-line CPI. With inflation trends now unclear (bounce back or not) and rates near new highs, growth must stay strong to keep stagflation concerns from spiking, and growth rolling over is now the key risk for markets. As mentioned, that means Retail Sales and Empire Manufacturing (today) and Philly Fed (tomorrow) need to show stability. Those data points won't spike stagflation worries by themselves, but growth is the lynchpin holding this market up, and it needs to stay strong because if stocks have to confront slowing growth and rates this high, the S&P 500 will drop, likely sharply.

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